COST OF LIVING ADJUSTMENT (COLA)

I. PURPOSE

The Purpose of this Statement of COLA Policy is to set forth the objectives and strategy of the Retirement Board for the Sonoma County Employees' Retirement Association (SCERA) with regard to COLAs for retired members and beneficiaries, as granted by the Sonoma County Board of Supervisors. The County of Sonoma has not adopted an on-going COLA program, and, as a result, the granting of such adjustments is a matter of discretion under Article 16.6 of the County Employees Retirement Law of 1937 (the Act, or '37 Act). As regards the exercise of that discretion, this document contains certain guidelines established by the Retirement Board to assist it in administering the COLA provisions of the Act in a consistent and efficient manner. This policy is not intended, and shall not be interpreted to alter or in any way limit the discretion vested in the Retirement Board by law with respect to any determinations relating to COLA adjustments, and the Board specifically reserves the right to modify the provisions of this Policy, as it may, from time to time, deem necessary.

II. COLA OBJECTIVES

The Retirement Board's primary COLA objectives, in order of importance, are to:

A. Maintain reserves sufficient to permit the payment of all COLAs that have been granted to SCERA retired members and beneficiaries;

B. Maintain the purchasing power of retirement benefits to the extent allowable under the '37 Act by annually analyzing SCERA reserves to determine whether the COLA can be fully funded and the funding status communicated to the Sonoma County Board of Supervisors; and

C. Minimize Employer contribution rate increases.

III. COLA BENEFIT GUIDELINES

This statement reflects the current policy of the Retirement Board and establishes guidelines for setting the amount of the new COLA for retired members and beneficiaries.

A. Adoption: The Retirement Board has authority to grant a COLA only when an analysis of SCERA reserves demonstrates the new COLA can be fully funded in accordance with Section III.D. If these conditions are met, a new COLA shall be approved by the Retirement Board generally at or prior to its February meeting, and sent to the Sonoma County Board of Supervisors for adoption. If SCERA's review of funding sources, as described in section III. D., results in the inability to communicate to the Board of Supervisors that a new COLA can be fully funded from SCERA reserves due to the insufficiency of those sources, SCERA will prepare a financial analysis of its reserve balances, estimated cost of a COLA, and benefit recipient loss of purchasing power and present it to the Retirement Board generally at or prior to its February meeting. SCERA will communicate the results of the analysis to the Board of Supervisors and the Sonoma County Association of Retired Employees.

B. Effective Date: The new COLA shall generally be effective April 1 of the year in which it is adopted, or as designated by the Retirement Board. This means that the first payment of the new COLA shall be with the checks for the month it is effective of that year.

C. All COLAs adopted by the Board of Supervisors shall be targeted to a specified group of retirement members and beneficiaries and shall be payable for the lifetime of those members and beneficiaries.

D. Funding: A new COLA shall be adopted only when it can be fully funded from Unapportioned Earnings, future COLA reserve or Interest Fluctuation Reserve amounts above the statutory limit of 1% of assets, as described in Section IV. Fully funded means that an amount equal to the present value of expected future payments under the new COLA is transferred to the COLA Reserve – Current at the time of adoption.

E. Benefit Structure: The COLA may consist of the following two types: 1) Purchasing Power Update alone or 2) Purchasing Power Update plus Across-the-board COLA for all annuitants.

    1. Purchasing Power Update: The COLA shall meet all of the requirements under Section 31874.6 of the '37 Act. This portion shall be issued to all annuitants whose Accumulated COLA Deficiency, as defined in Section VII, is greater than (a) the retirement allowance as increased by the sum of annual changes in the CPI, less (b) the Purchasing Power Target, as described in Section VI. For each qualified annuitant, the amount of this COLA shall be set to bring that annuitant's Purchasing Power, as defined in Section VII, up to the Purchasing Power Target.

    2. Across the Board COLA for all Annuitants: This COLA shall meet all of the requirements under Section 31870 of the '37 Act.

IV. DETERMINATION OF UNAPPORTIONED EARNINGS

Apportion interest crediting to Member, Employer and Annuitant reserves. Use the current interest crediting rate and procedure as set forth in the Interest Crediting and Reserve Policy.

If insufficient earnings, then:

1. First, draw down the COLA Reserve - Future.
2. Second, draw down the Interest Fluctuation Reserve.
3. Third, Track negative balance through the Negative Contingency Reserve.

After accounting for Market Stabilization Reserve changes and Cash Flows, if sufficient earnings and a balance remains, then:

1. First, apply to the Negative Contingency Reserve.
2. Second, bring the Interest Fluctuation Reserve to 3% of the Plan's Market Value of Assets.
3. Third, the balance equals Unapportioned Earnings.

V. USE OF UNAPPORTIONED EARNINGS

It is currently the intention of the Retirement Board to pay COLAs from Unapportioned Earnings. This will be accomplished by allocating these earnings to specific reserves and designations within SCERA in the order specified below unless otherwise determined by the Retirement Board. The specific reserves and designations are defined in Section VII.

Priority Order:

A. *The Cost of Living (COLA) Reserve - Current,* shall receive apportionments to the extent required, based upon the last Actuarial Study, to insure that all prior COLAs previously adopted by the Board of Supervisors are 100% funded. The prior COLA Funded Percentage is defined in Section VII.

B. *The COLA Reserve – Current* shall be increased from Unapportioned Earnings, if the remaining Unapportioned Earnings are sufficient to fully fund the new COLA (as described in Section III).

C. *The COLA Reserve – Future* shall receive apportionments as determined annually using the current CPI, to the extent required to pre-fund the effective Purchasing Power Target/Cost of Living Adjustment.

D. *The Employer Reserve* shall receive apportionments to the extent required by the Retirement Board, to assist with payment for existing benefits.

E. *The COLA Reserve – Current and the COLA Reserve - Future*, to the extent required, may be used to increase the Purchasing Power Target in accordance with Section VI.

F. *To Other Reserves,* all remaining Unapportioned Earnings may be allocated to any other reserves as needed.

VI. PURCHASING POWER TARGET

The Purchasing Power Target shall initially be set at 80%. Over the long term, the Retirement Board would like to achieve a point where all members retain 100% purchasing power. The Retirement Board reserves the right to review the Purchasing Power Target when the funds are available to pay for a New COLA at the increased Purchasing Power Target level. The Retirement Board does not intend to raise the Purchasing Power Target above 100% at any time.

VII. GLOSSARY OF TERMS

A. Accumulated COLA Deficiency: An amount that is the deficiency between (a) the retirement allowance as increased by the sum of annual changes in the CPI, less (b) the retirement allowance as increased by the actual COLAs granted. This is often expressed as a percentage ratio of [(a)-(b)]/(a)=%. This calculation is defined in Sections 31870, 31870.1 and 31874.6 of the '37 Act, and is used to determine whether an annuitant is eligible for a purchasing power COLA.

B. Actuarial Liability: The portion of the Present Value of Projected Benefits that is attributed to past years of service by the Actuarial Funding Method.

C. COLA Cost of Living Adjustment: An increase in a member's retirement benefit to partially or fully reflect a change in inflation since the member's retirement.

D. COLA Reserve - Current: This is a statutory reserve under the '37 Act. This reserve is used to pay for COLAs adopted by the Board of Supervisors.

E. Employer Reserve: This is the statutory reserve under the '37 Act. This reserve is used to calculate future Employer contributions to SCERA.

F. CPI: The Consumer Price Index for All Urban Consumers as provided by the Bureau of Labor Statistics for the San Francisco-Oakland-San Jose metropolitan area.

G. COLA Reserve - Future: This is a special reserve set up by the Retirement Board to allow for pre-funding of Future COLAs to the extent approved by the Retirement Board.

H. New COLA: COLAs adopted by the Board of Supervisors during the current Plan Year.

I. Prior COLA: COLAs adopted by the Board of Supervisors prior to the beginning of the current Plan Year.

J. Prior COLA Funded Percentage: The portion of Prior COLAs that are currently funded. This percentage is calculated as:

$$\frac{\text{COLA Reserve}}{\text{Prior COLA Liability}}$$

K. Prior COLA Liability: The present value, using the actuarial assumptions approved by the Retirement Board for the current Plan Year, of all Prior COLAs for all of SCERA's annuitants at the valuation date.

L. Purchasing Power: The ratio of the amount that the annuitants current monthly benefit can purchase to the amount that the annuitant could purchase at retirement with the benefit that the annuitant was then receiving. This ratio is calculated as:

$$\frac{\text{(Member's current monthly benefit as of December 31) divided by}}{\text{(Member's original monthly benefit) x (1+accumulated CPI through 12/31 of previous year)}}$$

For purposes of this calculation, the Member's current monthly benefit includes all Across-the-Board COLAs and all Purchasing Power Update COLAs adopted by the Board of Supervisors.

M. Unapportioned Earnings: Unapportioned Earnings above 3% of the Plan's Market Value of Assets are held as unreserved.

VII. REVIEW

The Board will review this policy at least every three (3) years to ensure it remains relevant and appropriate.

VIII. HISTORY

The Board adopted this policy on 5/20/1999.

Reviewed on 9/16/2010 and 10/16/2014.

Reviewed and revised on 11/21/2002, 1/20/2005, 5/17/2007, 6/22/2017, 10/25/2018, 2/18/2021, and 6/16/2021.